

TRUSTS & ESTATES[®]

ESTATE PLANNING & ADMINISTRATION

A Publication of Communication Channels Inc.

MAY 1987

Trust Investment and Asset Management: Banks vs. Other Managers

Valuations of Closely Held Stock



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5/21/87

TRUSTS & ESTATES

Volume 126, No. 5

Estate Planning and Administration Since 1904

MAY 1987

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New portfolio strategies and customer-oriented marketing techniques are the focus of those involved in trust investment and asset management, as they prove once and for all that bankers are competent money managers. Cover photo courtesy of Barnett Banks of Florida, Inc.

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Data Denies 'Myth of Mediocrity'

Continuing study provides across-the-board results that bank trust departments meet or surpass the performance of other managers

By THOMAS S. STEWART

President
Provident National Bank
Philadelphia, Pa.

"Study Shows One of the Best Kept Secrets Among Investment Professionals"

"Bank Investment Advisers Finally Get Some Respect"

"Bank Trust Departments Gaining New Reputation as Effective Money Managers"

"Bank Investments Outperform Advisers"

"Banks Hold the Hot Hand in Portfolio Management"

"Guess Who the Top Investment Managers Are Now?"

"Forget Hot Shot Financial Advisers and Mutual Funds. New Figures Show Your Assets May Grow Fastest Under Bank Management"

Those are just some of the headlines that have appeared over the past three years in publications around the country, ranging from the *Wall Street Journal* to the *Philadelphia Inquirer* to *U.S.A. Today* and *Medical Economics*. As a result of the efforts of the American Bankers Association, the word is beginning to get out: Banks do perform as well as or better than competing asset management firms such as mutual funds, investment advisers and insurance companies.

For the third consecutive year, the Asset Management Committee of the American Bankers Association commissioned the Silver Spring, Md. firm of CDA Investment Technologies, Inc. to

conduct a study which would uncover the true performance record of bank equity managers vis-a-vis the competition.

During recent years, bank investment managers have had to struggle with a negative public perception — that they are poor performers when it comes to investment returns. We were thought to be stodgy, conservative investors. But bank investment managers themselves have felt this "myth of mediocrity" to be groundless and, once again, the CDA study has confirmed that indeed, it is a myth.

Before looking at the actual results, certain facts must be taken into account when evaluating bank performance: (1) A reasonable portion of investment assets under bank management (i.e., trust accounts) must be kept in relatively low-risk investments; (2) Parties involved in

a trust often have different investment objectives; and (3) Steady — not sporadically spectacular — performance is usually the bank's goal.

With those considerations in mind, it is even more gratifying to see that bank equity funds performed so well compared to the competition.

Survey Results

The 1986 study compared 306 bank-managed equity funds, 83 insurance company separate and variable accounts, 370 growth and growth-and-income mutual funds and 369 investment advisory accounts, with combined assets of \$577.4 billion. This is a larger, more representative survey than that of the two prior years, both in terms of the number of accounts measured and the market value of the combined assets of the accounts. The universe is selected by the CDA firm with the intention of identifying funds which have similar objectives and are comprised mostly of equities — to make comparisons meaningful and accurate.

As in previous years, bank trust departments continue to meet or surpass the performance of insurance companies, mutual funds and investment advisers in managing their client's money.

"Banks compared favorably and exhibited greater consistency among managers than did mutual funds and investment advisers," said Robert Levy, pres-

Banks compared favorably and exhibited greater consistency among managers than did mutual funds and investment advisers.

ident of CDA. "For example, the three-year median returns shows that a typical bank outperformed 59 percent of all managers, while the five-year medians show a typical bank outperformed 53 percent of those managers," Levy said.

The CDA study proves that banks' strong investment performance is a fact, not a fad. Any lingering criticism inferring that banks are poor investment managers is finally erased by the across-the-board results of this study and the study from the previous two years.

Several major findings can be extracted from the study:

1. Banks and insurance companies had higher annualized rates of return for the three- and five-year periods, compared to mutual funds and investment advisers.

2. Banks performed well during the most recent stock market cycle. That is, they declined less than others during the bear market phase and increased in line with other types of managers during the bull market portion of the cycle.

3. Banks showed greater consistency among managers. That is, there is less variation in performance than other classes of managers. Thus, relying on a bank for investment management increases the likelihood of a more predictable result. (See Table 1.)

Changing Perceptions

It is the opinion of the ABA that this need for clarification of bank investment performance is a long-standing problem. It is something that must be addressed year after year with the greatest emphasis being placed on the *communication* of the study's results. To that end, the current ABA plan is to use the data in several ways:

1. The results of the study are being included in the ABA's legislative efforts. By demonstrating the highly competitive investment results achieved

Any lingering criticism inferring that banks are poor investment managers is finally erased by the across-the-board results of this study.

by bank investment managers, the ABA will attempt to prove that it is in the consumer's best interest to allow banks to receive expanded powers, such as in the area of directly offering mutual funds.

2. The financial press is receiving press releases on the study as well as full copies of the report. This effort is being stepped up this year and resulting press coverage is being tracked more closely.

3. Employee benefit and investment consultants are being notified of the results to enable them to become more familiar with bank performance, in hopes that they will include banks among the managers they recommend.

4. Plan sponsors and administrators of the companies in the Fortune 1001-2000 range are being apprised of the results, with the thought that they may be a receptive audience to bank investment management.

All of these efforts by the ABA are certainly beneficial to our industry, but in order to make a meaningful difference in one bank's marketplace, it is critical for bankers to get the message out in their own way. Particularly if a specific bank has better performance numbers than the averages used in the study!

The ABA provides the study as a service to its members. With the results of

the study in hand, it can serve as a powerful marketing tool and should be used as such.

Local Marketing

What are some ways you can use it? Get a copy of the release describing the study (call Mary-Liz Meany at the ABA: 202-663-5465) and deliver it to your local paper with a cover letter from your trust department manager, describing your own bank's performance — if you are comfortable with it — or some other angle that adds a local element to the study. Better yet, offer to write an article for a local publication using the results of the study as a theme. Local publications, especially small community papers, are always in need of copy for their next deadline. And once it appears, you can reprint it with their permission, and hand it out or mail it whenever appropriate.

Run an advertisement highlighting the study or make available to your clients and prospects a summary sheet which lists your bank's investment performance compared to the averages in the study. We do that at Provident as part of our ongoing presentation of investment performance and right now, these sheets are on display in the frames we have placed inside our building elevators. After all, our first target of communication has to be our own employees to whom we disseminate information consistently, through in-house newsletters, article reprints and performance bulletins.

And don't restrict such communication to the officers in your trust department only! Everyone from senior management to lending officers to branch personnel has important client contact and should be aware of your investment abilities so that they, too, can be spreading the word of your competence.

Just as you should communicate consistently with your staff (repeat, repeat, repeat) you must tell your clients of your success and the methods used to achieve them. Although many of your clients may be more interested in your personal service than they are in their actual investment returns, it is important that you make the effort to tell them about their investments. One way to reach them may be through their attorney — another vitally important audience for your communications effort.

Use Attorneys

As mentioned in the March TRUSTS & ESTATES article by David Nutt of U.S.

TABLE 1

Annualized Rates of Return
for Periods ended 12/31/85

	3 yrs.	5 yrs.	10 yrs.
Banks	17.0%	19.3%	13.7%
Insurance Companies	17.4	19.6	13.9
Mutual Funds	14.6	17.8	13.8
Investment Advisers	16.2	18.4	n/a
S&P 500	18.4	19.8	13.8

Source: CDA Investment Technologies, Inc.

Be sure your management understands the importance of a professional investment product and that it is well articulated and presented.

Trust, many attorneys view themselves as investment consultants to their clients — just as the Frank Russell group is in the pension field. They need to be well-informed of the investment capabilities of the firms they recommend to clients, feeling comfortable with the performance, the method used to achieve that performance and the relative standing of the managers vis-a-vis their competitors. Once again, the CDA investment performance study can be an effective tool in communicating and building a relationship with this all-important center of influence.

This may be just the right audience that would appreciate hearing some explanation behind the achievement of the bank performance, as noted in the study. In the recent market cycle, traditional trust department-type investing has paid off handsomely, as the larger Dow Jones-type stocks have far outperformed the small cap stocks. Secondly, going forward, the trust department's orientation toward *investing for income* will be just as advantageous as *investing for capital gains*, since the new tax law regards both equally from a tax perspective.

Using such points as part of your marketing effort to attorneys (and CPAs and financial planners) is likely to be well-received. Good marketing efforts will be respected by law firms, particularly, as they themselves continue to engage in strategic planning to expand their businesses.

Emphasize Quality

What if your investment numbers are not as good as the averages and you feel uncomfortable highlighting the quantitative side of your business? If that is the case, you should emphasize the qualitative aspects of your investment services. Be sure your management understands the importance of a professional investment product and that it is well-articulated and presented. Be sure

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Different clients have vastly different investment objectives and although the best rate of return may not be necessary to meet a client's objectives, it is a difficult job for sales professionals to compete today without strength in the investment area. With the competition that exists for consumers' investment dollars today a solid investment product is needed to retain business you already have as well as to gain new business. Without it, there are plenty of other organizations that will win investors' dollars by eagerly pursuing them with a commitment to a successful investment process.

Fortunately, for some bank trust departments particularly small and medium-sized departments, there are several alternatives available which can lend support to an institution's investment capability.

At Provident we have spent more than 20 years building an investment team with a well-articulated philosophy of value-oriented investing. We have made a commitment to creating a strong investment research group as well as a cadre of portfolio managers. Our next step is to form a funds management unit, which will manage a complete, diversified family of common trust funds for all PNC Financial Corp. affiliates and their clients. This is feasible and expected for an organization our size, but it may not be practical for many organizations.

Companies such as PNC are in the business of sharing their investment expertise for a fee — either by selling the original research they produce or actually advising the client bank on its portfolio management. Some organizations (including PNC) are even in the business of actually managing a piece of another bank's client portfolio (sort of a subcontractor relationship.) Bankers should assess their own in-house investment capabilities and determine whether they should buy services from other institutions.

There are excellent alternatives available today and many banks have taken advantage of them. The purchase of

*We encourage all
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mutual funds managed by other companies is just one example of the way banks are buying investment services today. This is very acceptable practice, both from a regulatory point of view as well as from the client's standpoint. It is essential for the institution that wants to offer a broad array of diversified investments to satisfy clients' needs, but doesn't have the resources to offer its own family of funds.

What alternatives lie ahead? We have already seen several banks establish commingled funds for IRA investing, which are also registered with the Securities and Exchange Commission. We are seeing some states offer legislation that allows interstate and intrastate investment in common trust funds, within a bank holding company. And we are seeing more and more banks get their feet wet in the mutual fund business by serving as the investment adviser to a fund's distributor. All of these are possible ways for an institution to provide investment strength. There are numerous other alternatives.

As you know, the bank component of the CDA study is comprised of 306 commingled funds managed by bank trust departments. In my opinion, it is the common trust fund vehicle that provides one of the very best investment opportunities to the affluent investor. The pooled fund offers full-time management, excellent diversification and economies of scale. At Provident, we encourage all our clients to consider investing in the funds and we showcase the funds as our premier investment vehicles. ☐

Thomas S. Stewart is an Executive Vice President in charge of the Trust Division of Provident National Bank, Philadelphia. He is coordinator of all trust activities for PNC Financial Corp. and is Chairman of the Asset Management Committee of the American Bankers Association.